

Internal Revenue Service

memorandum

WHEARD CC:TL:TS

TL-N-5465-90

date: JUN 25 1990

to: District Counsel, Dallas CC:DAL
Attn: Jere Blackshear

from: Assistant Chief Counsel (Tax Litigation) CC:TL

subject: [REDACTED]

TL-N-2303-90

CC:TL:TS Heard Wilson

I.R.C. §§ 6501, 6229(f)

Which Statute of Limitations Applies

This memorandum is in response to your request for tax litigation advice received April 4, 1990.

ISSUE

Whether the period for assessment under I.R.C. § 6501 or under section 6229(f) applies to the [REDACTED] taxable year of partners who filed for bankruptcy in [REDACTED].

CONCLUSION

Generally, the period for assessing partnership items which have converted to nonpartnership items is section 6229(f). On a case by case basis, however, we will authorize assessment within the period provided for by section 6501(a) as long as this period is open other than through a statute extension (Form 872).

A notice of deficiency may be issued within the section 6501(a) period for assessment if this period is open other than through a statute extension (Form 872) if the Service did not receive actual or constructive notice of the petition in bankruptcy within a reasonable time after the filing of the petition in bankruptcy, e.g., if the Service was not listed as a creditor to whom notice of the bankruptcy proceeding was sent and the Service did not receive notice of the proceeding until late in the one year period or after this period had expired.

A notice of deficiency may also be issued if the period for assessment under section 6229(f) expired less than one year after the [REDACTED] filed their return and the three year period for assessment under section 6501(a) is open because the [REDACTED] filed their return late.

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FACTS

_____ was a partner in _____ Joint Venture, a TEFRA partnership for the _____ taxable year. On _____, _____ and his wife filed a petition in bankruptcy under Title 7 of the Bankruptcy Code. The Examination Division has stated that the section 6501 statute will expire on _____. They have not stated whether this statute date was extended beyond the normal section 6501 three year assessment period ending on _____ because the return was filed late or because a statute extension was executed.

DISCUSSION

Initially we note that the partnership items for the _____ taxable year converted to nonpartnership items on the date the _____ filed for bankruptcy. I.R.C. §§ 6231(b)(1)(e) and 6231(c); Temp. Treas. Reg. § 301.6231(c)-7T(a).

The period for assessing partnership items which have converted to nonpartnership items is specifically provided by section 6229(f) which provides as relevant here:

(f) Items Becoming Nonpartnership Items.-If, before the expiration of the period otherwise provided in this section for assessing tax imposed by subtitle A with respect to the partnership items of a partner for the partnership taxable year, such items become nonpartnership items by reason of one or more of the events described in subsection (b) of section 6231, the period for assessing any tax imposed by subtitle A which is attributable to such items (or any item affected by such items) shall not expire before the date which is 1 year after the date on which the items become nonpartnership items. . . .

This office has advised the Examination and Appeals Divisions that assessments of converted partnership items should be assessed within the one year period provided by section 6229(f). This is consistent with our general position that Congress intended to provide a separate statute of limitations with respect to partnership items under section 6229. This conservative "separate statute" approach was adopted to foster protection against expired periods of limitation. On a case by

case basis, however, we are willing to recommend defense of assessments made after the period under section 6229(f) has expired but within the period provided for by section 6501(a).

The legal basis for arguing that section 6501 applies to partnership items which have converted to nonpartnership items is as follows: Section 6231(b) provides that in certain circumstances, partnership items "shall become" nonpartnership items. Since, nonpartnership items are subject to the period for assessment under section 6501, we will take the position in appropriate cases that partnership items which are converted to nonpartnership items are subject to the period of limitations under section 6501. See Tax Litigation Guideline T1-81.

Congress provided the additional one year period of section 6229(f) to give the Service at least one year to assess after conversion. Events may occur which will operate to convert partnership items with little time left on the section 6501 period or after the period for assessment under section 6501 has expired. In other cases, it may be impossible to assess converted items within the period provided under section 6229(f) necessitating reliance on section 6501.

For instance, a settlement agreement converts partnership items to nonpartnership items. I.R.C. § 6231(b)(1)(C). Where a settlement agreement covers future years, the period under section 6229(f) could expire less than one year after the partner's personal tax return is due or even before the taxes for that year become legally due and owing. It is also possible to have the period under section 6229(f) expire less than one year after personal returns are due in other types of conversion situations. See, e.g., I.R.C. § 6231(c); Temp. Treas. Reg. § 301.6231(c)-7T (bankruptcy conversion). Thus, at least with respect to sections 6501 and 6229(f), the Service subscribes to a "statute extension" interpretation on a case by case basis where it is impossible or difficult to assess within the one year period following conversion of section 6229(f).

Where the one year period for assessment under section 6229(f) will expire less than one year from the date a partner's return is due (determined with regard to any extension), we generally recommend defending assessments made within the period provided by section 6501(a). For instance, a partner might file a petition in bankruptcy on January 1, 1990. He obtains an automatic extension to August 15, 1990 and timely files his return for the 1989 taxable year on that date. The one year period for assessment under section 6229(f) would expire on January 1, 1991 of the following year, four and one-half months after the return is due. Because we do not believe Congress intended such a result, such cases present favorable facts for advancing a "statute extension" interpretation of section

6229(f). Under that interpretation section 6229(f) extends the period of limitations for one year if the otherwise applicable period under section 6501 would expire earlier.

The years which convert pursuant to Temp. Treas. § 301.6231(c)-7T are years for which "the United States could file a claim for income tax due" in the bankruptcy proceeding. With respect to taxable years ending before the date of filing, a claim for income tax due may be filed immediately upon the filing of the petition. Thus, all taxable years ending before the date of the bankruptcy petition will convert upon the filing of the bankruptcy petition.^{1/}

We may also recommend defense of assessments which are made more than one year after a partner's return is due if the Service is not informed of the converting event. Generally, the Service is informed by the bankruptcy courts of bankruptcy filings by a taxpayer in Title 11 or Title 13 cases but not in Title 7 cases. Where the Service receives notice of the bankruptcy, this information is entered into the Master File Computer and is then available to the various branches of the Service through a computer inquiry. Sometimes, the entry into the Master File Computer may be delayed for some time. Nevertheless, the branch of the Service with responsibility for assessing a bankrupt partner will have constructive notice of the bankruptcy once a reasonable time for entering the information has passed, even if the information is not entered into the Master File Computer until later.

In the instant case, the [redacted] filed a petition in bankruptcy on [redacted]. We have been unable to determine whether the [redacted] section 6501 statute expires on [redacted] because they filed their return late or whether it is open through a statute extension (Form 872). If they did not file a return until after the date of the petition in bankruptcy, then

^{1/} Post-petition years may also convert for years in which the bankruptcy estate (rather than the debtor) generates taxable income, and thus, a claim can be filed for these years. Since the Service will not know the amount of the liability for post-petition years which have converted until a return is filed for those years, we have taken the position (in this situation only) that post petition years for which a claim for income tax due may be filed in the bankruptcy court will not convert until a partner's tax liability for that year becomes legally due and owing. A partner's tax liability will not become "due and owing" until the last date for payment of the taxes in question. Mendenall v. United States, 72-1 USTC par. 9431; see also United States v. Northwestern Mutual Insurance Co., 315 F.2d 723 (9th Cir. 1963).

the one year period for assessment under the separate statute interpretation of section 6229(f) would expire less than one year from the date their return was filed. Thus, if the return was filed after [REDACTED], you may recommend issuance of a notice of deficiency for the converted items prior to the expiration of the three year period for assessment under section 6501(a) if this period is open because of a late filing, rather than through a statute extension (Form 872).²

Alternatively, if the Service did not receive actual or constructive notice of the petition in bankruptcy before the one year period under section 6229(f) expired or otherwise did not receive such notice of the bankruptcy within a reasonable time after the filing of the petition in bankruptcy, you may recommend issuance of a notice of deficiency prior to the expiration of the unextended period for assessment under section 6501(a).

In summary, we recommend that assessment of converted items or issuance of a notice of deficiency for such items take place within one year of the date of conversion pursuant to section 6229(f). If the one year assessment date has expired, we may authorize the issuance of a notice of deficiency within the period of section 6501(a) if it is open other than through a Form 872, on a case by case basis. Factual circumstances under which we will authorize the use of section 6501 generally are where the one year period under section 6229(f) will expire less than a year after the tax return for the year in question is filed or where the Service is not informed of the converting event within a reasonable time, e.g., when the Service is not listed as a creditor to whom notice of the bankruptcy proceeding is sent and the Service does not receive notice of the proceeding until late in the one year period or after this period has expired.

If your facts fall under one of the above scenarios, we recommend defending the issuance of a notice of deficiency within the period for assessment of section 6501(a) if it is open other than through a Form 872 statute extension.

² Section 6229(b)(2) provides that an extension under section 6501(c)(4) shall not apply to partnership items unless these items are specifically referenced in the extension. Where an extension initially does not apply to the partnership items, it will not retroactively become applicable to partnership items after they have converted; the intent of the agreement at the time it is executed, as impacted by section 6229(b)(2), would control. Arguably, however, an extension under section 6501(c)(4) should be valid with respect to partnership items which converted prior to the execution of the extension under section 6501(c)(4) since they would be nonpartnership items at the time the extension was executed.

Please refer any questions on this matter to Bill Heard at
FTS 566-3289.

MARLENE GROSS

By:

A handwritten signature in dark ink, appearing to read "Curtis G. Wilson", is written over a horizontal line.

CURTIS G. WILSON

Acting Chief, Tax Shelter Branch